ANNUAL REPORT 1963

RJR

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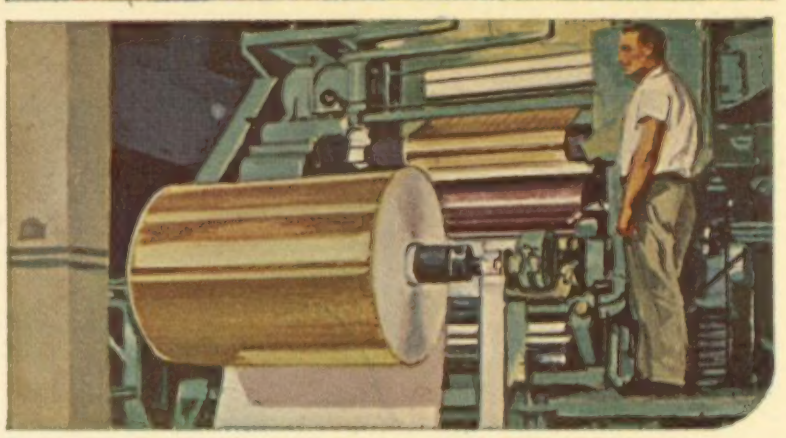

R. J. REYNOLDS TOBACCO COMPANY

R. J. REYNOLDS TOBACCO COMPANY

WINSTON-SALEM • NORTH CAROLINA

RJR

PRINCIPAL PRODUCTS

CIGARETTES

Camel

Winston

Salem

Cavalier

SMOKING TOBACCOS

Prince Albert

George Washington

Carter Hall

Top

CHEWING TOBACCOS

Days Work

Brown's Mule

Apple Sun Cured

Reynolds' Natural Leaf

ARCHER ALUMINUM DIVISION

Foil Products

Packaging Materials

PACIFIC HAWAIIAN PRODUCTS COMPANY

Hawaiian Punch

King of the Islands Exotic Drinks

Cinch Bread and Cake Mixes

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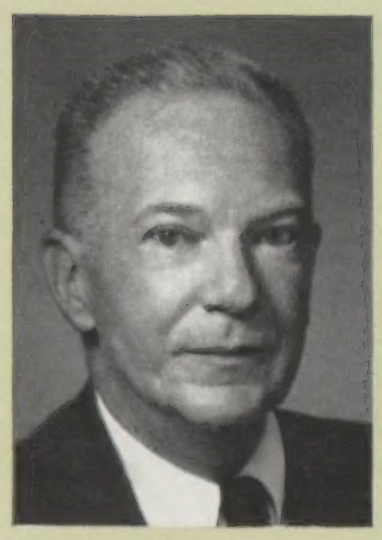
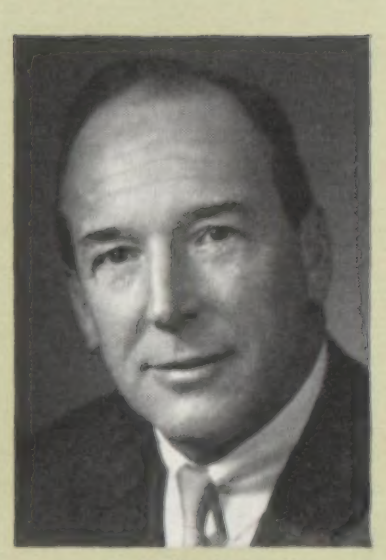
TO THE STOCKHOLDERS



Bowman Gray



A. H. Galloway

The Company's business during 1963 reached the highest level in its history. New highs were attained in sales, earnings and dividend payments. In addition to being the largest producer of cigarettes for the domestic market, the Company has become the leading exporter of cigarettes from the United States.

Net earnings were 6.5 per cent higher than 1962, the previous record year, and sales were 2.8 per cent higher. The dividend rate on the Common Stock was increased to 45 cents per share in the last quarter, making the tenth consecutive year in which the rate has been raised.

The number of cigarettes sold by the Company also reached a new high, due principally to the strong performance of WINSTON, the leading filter brand in the country. SALEM, the leading menthol-flavored cigarette, maintained its position in the face of a barrage of new, competing brands. CAMEL remained the leading regular-size, non-filter cigarette, increasing its share of that market although volume declined.

Like all members of the tobacco industry – which includes growers, warehousemen, processors, suppliers, manufacturers, distributors, and retailers – the Company is confronted with problems resulting from the report of the Surgeon General's Committee on Smoking and Health which was released on January 11, 1964. It will face these problems realistically in a continuing effort to do what is best for the users of its products, for its stockholders and employees, for the communities in which it operates, and for the industry of which it is a part. It will continue to support an intensified research program designed to find truly scientific answers to the complex problems of smoking and health – from the growing and processing of tobacco to the methods of its use. It is confident that the combined efforts of government and the industry will eventually point the way to a solution, equally satisfactory from the standpoint of public health and the tobacco business.

As pointed out in the Financial Review elsewhere in this report, the Company's year-end inventories were noticeably lower because of the earlier closing of the Burley leaf tobacco markets in 1963. Since the reopening of these markets in January of this year, the Company has substantially completed acquisition of its Burley tobacco requirements, restoring its inventory position to a more normal basis.

The experience of the Company in working with its new subsidiary, Pacific Hawaiian Products Company, continues to be pleasant and profitable. Again in 1963, this organization materially expanded its sales and earnings. The contributions made by its executives and employees have been most helpful to the Company's over-all performance and its progress in diversification.

The tobacco business has never been without its challenges. In the past year, our employees at all levels have met these challenges with loyalty and rededicated effort. On behalf of the Board of Directors, we express our appreciation for their help in making 1963 the best year in the Company's history. With their continued help, we are confident that this progress will be sustained.

Respectfully submitted for the Board of Directors,

Chairman, Board of Directors

President

February 6, 1964

RJR

COMPARATIVE SUMMARY

CONSOLIDATED

SALES, EARNINGS AND DIVIDENDS	1963	1962
Net Sales	$1,672,444,707	$1,627,541,446
Net Earnings	129,065,759	121,156,165
Net Earnings as a percentage of Net Sales	7.72%	7.44%
Earnings per share on Common Stock *before* taxes on income*	$ 6.75	$ 6.34
Taxes on income per share of Common Stock*	3.62	3.41
Net Earnings per share of Common Stock*	3.13	2.93
Dividends per share on Common Stock	1.65	1.60
Dividends on Preferred Stock	857,898	936,486
Dividends on Common Stock	67,602,086	64,512,422

*Based on 40,971,533 shares

FINANCIAL POSITION AND EQUITIES AT YEAR END		
Total Assets	$1,037,639,534	$1,089,126,876
Current Assets	878,115,844	930,245,857
Current Liabilities	257,995,847	361,832,463
Net Current Assets–Working Capital	620,119,997	568,413,394
Real Estate, Machinery and Equipment–Net	150,023,031	147,568,044
Funded Debt	68,000,000	74,000,000
Equity of holders of Preferred Stock	22,459,000	24,974,700
Equity of holders of Common Stock	689,184,687	628,319,713
Number of stockholders at year end	103,282	102,040
Number of regular employees at year end	14,932	15,813

FINANCIAL REVIEW

Sales in 1963 were $1,672,444,707, an increase of 2.8 per cent or $44,903,261 over 1962. Net earnings were $129,065,759, or $7,909,594 greater than in the previous year, an increase of 6.5 per cent.

Net earnings on the Common Stock, after payment of dividends on the Preferred Stock, amounted to $3.13 per share compared with $2.93 in 1962, based on 40,971,533 issued shares.

The 1963 figures are consolidated to include those of Pacific Hawaiian Products Company, acquired in February, and the 1962 figures have been adjusted accordingly.

In the fourth quarter of 1963, the quarterly dividend on Common Stock was increased from 40 cents to 45 cents per share, resulting in a total of $1.65 a share for the year compared to $1.60 during 1962. Dividends amounted to $67,602,086 on the Common Stock and $857,898 on the Preferred Stock, a total of $68,459,984, the largest for any year in the Company's history.

At year end, short-term borrowings were $114,500,000, or $107,850,000 less than at the close of the previous year, and inventories totaled $795,565,237 against $845,928,451 at the end of 1962. As there were fewer marketing days in 1963 for the Burley tobacco crop, a much smaller part of the crop was sold prior to December 31 than has been the case in recent years. Consequently, the Company's purchases were substantially less than they otherwise would have been, resulting in an estimated reduction at the year end of $28,000,000 in inventories and an equivalent reduction in short-term borrowings.

Due to smaller average borrowings during the year, interest and debt expense amounted to $7,131,586 compared to $8,857,354 in 1962. Short-term borrowings reached a low point of $26,500,000 in 1963 compared with $75,000,000 in the previous year.

Capital expenditures during the year amounted to $21,940,268, principally in connection with increasing steam and electric power generating capacity, continuing modernization of cigarette and processing plants and equipment, and

DISPOSITION OF 1963 NET EARNINGS

Dividends paid	$ 68,459,984
Purchase of Preferred Stock, 3.60% series	2,213,840
Purchase of Common Stock	42,661
Reduction in funded debt	6,000,000
Net addition to plant and equipment	2,454,987
Increase in working capital	51,706,603
	$130,878,075
Less decrease in other assets	1,812,316
Net earnings	$129,065,759

COMPUTATION OF INCREASE IN WORKING CAPITAL

Decrease in current liabilities	$103,836,616
Less decrease in current assets	52,130,013
Increase in working capital	$ 51,706,603

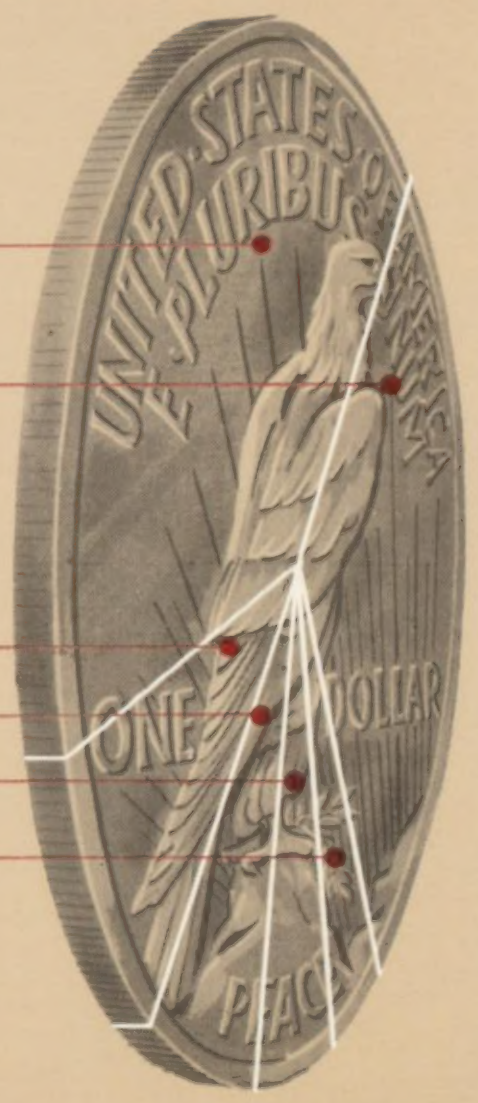
expanding facilities for the Archer Aluminum division. Expenditures for plant expansion and improvements in 1964 are presently estimated at $16,000,000.

Depreciation charges amounted to $18,338,525 compared with $15,648,401 for the preceding year. These charges included amounts of $1,684,513 and $1,134,369, respectively, equivalent to the investment credits permitted under the Federal tax laws pertaining to the purchase of new machinery and equipment. After deducting accumulated depreciation and adjusting for disposals, the net account for real estate, machinery and equipment stood at $150,023,031, or $2,454,987 more than at the end of 1962.

In 1963 funded debt was reduced by $6,000,000. During the year, the Company purchased for its treasury an additional 25,157 shares of its Preferred Stock at an average cost of $88 per share.

On February 14, 1963, the Company issued 971,533 shares of its Common Stock in acquiring the business of Pacific Hawaiian Products Company, which is

DISTRIBUTION OF THE 1963 SALES DOLLAR



42.5¢ EXCISE TAXES

34.5¢ LEAF TOBACCO, OTHER MANUFACTURING COSTS AND FREIGHT

8.9¢ TAXES ON INCOME

6.4¢ SELLING, ADVERTISING, ADMINISTRATIVE, INTEREST AND OTHER EXPENSES

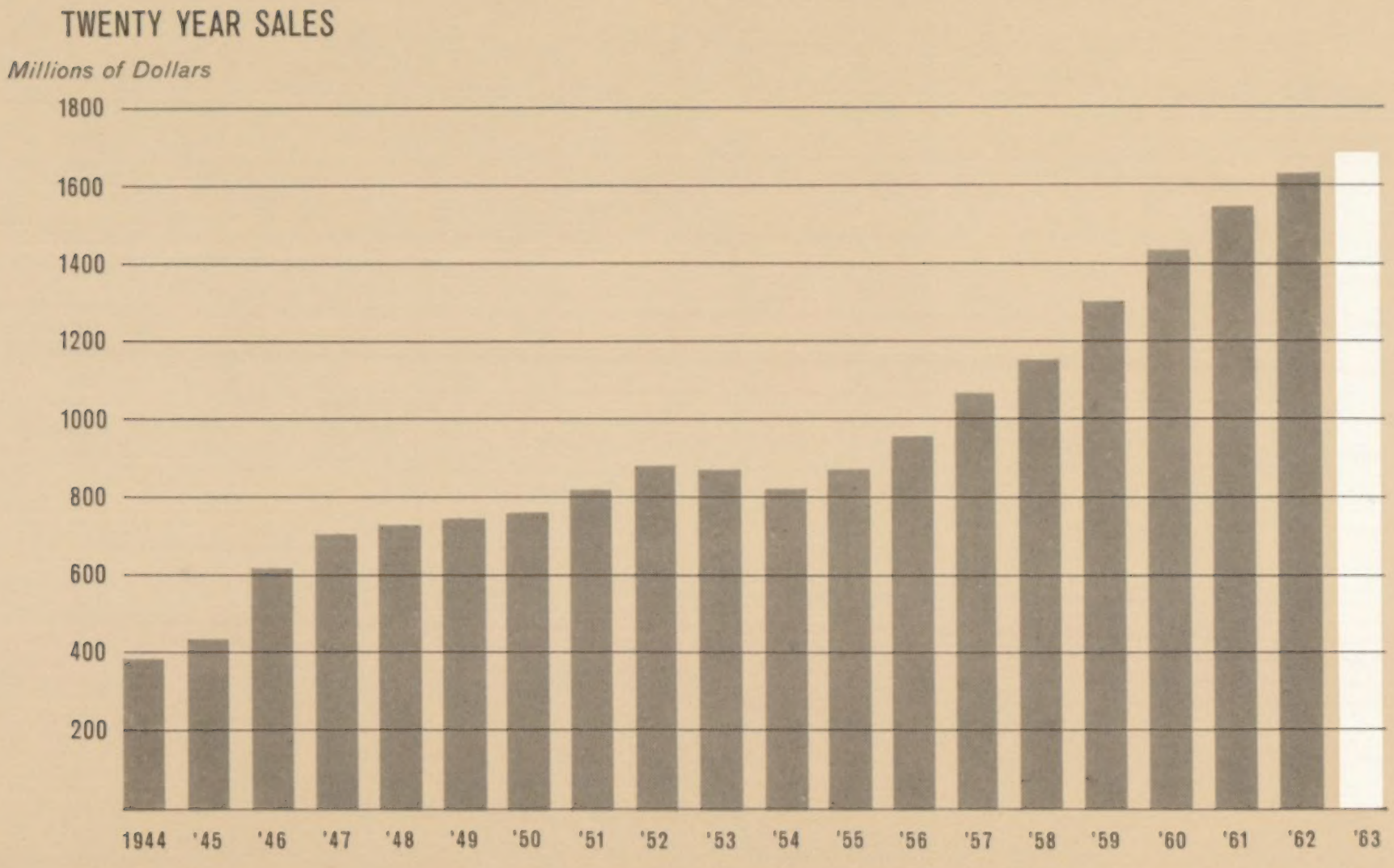
4.1¢ DIVIDENDS

3.6¢ EARNINGS RETAINED

being operated as a subsidiary.

Accounts of foreign affiliates are not consolidated with those of the Company. The Company's share of net earnings of its 51-percent-owned West German affiliate, Zigarettenfabrik Haus Neuerburg K. G., amounted to $600,000, including $317,000 resulting from the sale of a surplus factory building and real estate. This amount has been reflected in income for the year with a corresponding reduction in the Reserve for Losses of Unconsolidated Foreign Affiliates.

During the past seven years of major plant expansion, the net account for real estate, machinery and equipment has been increased by $104,224,000. In the same period, working capital has been increased by $155,248,000 and other assets by $6,117,000. Funded debt has been reduced by $42,000,000, and an additional $43,724,000 has been spent for the retirement and acquisition of Preferred Stock. During these seven years the stockholders' equity per share of Common Stock has increased from $8.20 to $16.82.



MARKETING

In 1963 the Company continued as the largest producer of cigarettes for both the domestic and the export markets. Three of the four best-selling cigarette brands in the nation were Reynolds products.

WINSTON, believed to have had the greatest volume gain of any cigarette in the industry, is now the Company's largest-selling brand. WINSTON is America's favorite filter cigarette and is second in sales among all cigarettes.

CAMEL remained the leading regular-size, non-filter cigarette. It improved its share of this market, although declining somewhat in total volume in line with the industry trend toward filters. CAMEL ranked third last year in national brand standings.

SALEM, the top-selling menthol cigarette, increased in volume and was fourth among all brands. It is the second largest-selling filter cigarette.

The Company's smoking and chewing tobacco sales were slightly lower in 1963, as was true for the industry. PRINCE ALBERT remained the nation's best-selling brand of smoking tobacco, and CARTER HALL showed a substantial increase in volume. DAYS WORK retained the top position among chewing tobaccos.

ADVERTISING PROGRAM

An effective advertising program contributed to the Company's continued sales leadership in the face of increased competition and the challenge of new products.

In promoting its products on network television the Company shared in the sponsorship of a wide range of programs. The comedy hit, *The Beverly Hillbillies,* continued to attract the largest audience of any network show. *The Huntley-Brinkley Report* received the 1963 "Emmy" Award of the National Academy of Television Arts and Sciences for outstanding achievement in the field of news.

Other network TV shows used to advertise the Company's products to nationwide audiences included *McHale's Navy,* a popular comedy show; *To Tell the Truth* and *Password,* panel shows; *Wagon*

An important factor in the Company's sales leadership is the widespread distribution of its products through retail outlets. Wherever cigarettes are sold—at newsstands, in supermarkets and grocery stores, drug stores and tobacco shops, in vending machines and many other locations—the Company's major brands are readily available.

Train, a western drama; *The Garry Moore Show,* a long-time variety favorite; *Glynis,* mystery comedy, and *77 Sunset Strip,* mystery drama; *The Lieutenant,* an adventure series; and *Saturday Night at the Movies.*

In selected markets, added promotional support was provided by television spot announcements. Radio coverage consisted of local and network spots.

During the year there was an extensive newspaper campaign for WINSTON. It introduced a new advertising theme: "Changing to a filter cigarette? Change to WINSTON! – America's largest-selling filter cigarette."

A strong schedule of advertising in a long list of widely read magazines was maintained throughout the year in support of various brands. A "different look" in magazine advertising was created for WINSTON, making use of very simple and attractive illustrations. *(An example appears on the back cover of this report.)*

Recognizing that smoking is a custom for adults and a matter for mature decision, the Company designs its advertising to appeal to the adult market.

SALES ORGANIZATION

The Company is believed to have the largest sales force in the tobacco industry. With a careful eye to population shifts, certain realignments were made last year in the field sales organization to keep it at top strength and efficiency.

Each salesman is charged with the responsibility of calling on all wholesalers and retailers in his territory who sell tobacco products. Service to its customers continues to be the Company's basic marketing philosophy, with the aim of helping them to sell more Reynolds products.

INTERNATIONAL MARKETS

The Company again substantially increased its volume and share of the market for cigarettes exported from the United States. Recognizing the prestige and growing acceptance of American-made cigarettes, the Company continued to increase its manpower, advertising, and promotional efforts in many countries throughout the world.

In export as in domestic sales, filter cigarettes were the large growth segment, with the Company's filter brands showing particular strength in capitalizing on the developing world-wide trend to filters.

Zigarettenfabrik Haus Neuerburg, K.G., the Company's affiliate in West Germany, again improved its share of the market in the non-filter category with OVERSTOLZ, its leading brand. REYNO retained its leadership in the menthol-filter field and showed a gain in volume for the year. Development of new filter brands received close attention, in the continuing effort to improve Haus Neuerburg's position in this important and growing category.

Railway express trucks carry colorful posters featuring the Company's popular brands.

Car cards, with pertinent selling themes, catch the eyes of rail and subway passengers.

TOBACCO PRODUCTS

CIGARETTES

Camel
Winston
Salem
Cavalier

SMOKING TOBACCOS

Prince Albert
George Washington
Carter Hall
Top

PRINCIPAL BRANDS OF CHEWING TOBACCOS
(not illustrated)

Days Work
Brown's Mule
Apple Sun Cured
Reynolds' Natural Leaf

PACIFIC HAWAIIAN PRODUCTS COMPANY

Reuben P. Hughes
President

Pacific Hawaiian Products Company, the Company's newest subsidiary, has its headquarters and main production facilities in Fullerton, California. It produces non-carbonated fruit juice beverages, the most prominent brand being HAWAIIAN PUNCH, which is marketed in ready-to-drink form in cans, in concentrate form in bottles and cans, and in frozen-concentrate form in cans. In addition to HAWAIIAN PUNCH, a line of exotic tropical juices is sold under the KING OF THE ISLANDS brand.

An affiliate of Pacific Hawaiian produces a line of bread and cake mixes, which have regional distribution on the West Coast under the trade-mark CINCH.

During 1963 KING STIR, a carbonated instant soft drink, was successfully test-marketed on a limited basis. Plans are being made to expand the market test in the summer of 1964, KING STIR being a seasonal item. Other new products are being developed for marketing by Pacific Hawaiian.

The products of Pacific Hawaiian are marketed through food brokers under the supervision of Pacific Hawaiian's own sales organization, which is entirely separate from R. J. Reynolds Tobacco Company's sales force.

Sales and earnings increased substantially in 1963 over the previous year, and continued growth is expected. For Pacific Hawaiian and its subsidiaries, sales amounted to $30,692,666, an increase of 25% over 1962, and net earnings were $1,796,649 or 33% higher.

Modern plant facilities and general offices of Pacific Hawaiian Products Company at Fullerton, California

Pacific Hawaiian products now in national distribution include HAWAIIAN PUNCH in ready-to-drink form in 46-ounce cans *(Rosy Red* and *Sunshine Yellow)* and in carry-home cartons of six 12-ounce cans *(Rosy Red);* in frozen-concentrate form in 6-ounce cans *(Rosy Red).*

Available in selected areas are *Sunshine Yellow* HAWAIIAN PUNCH frozen concentrate and *Rosy Red* HAWAIIAN PUNCH liquid concentrate; and KING OF THE ISLANDS Exotic Drinks in three flavors of fresh-frozen concentrate.

ARCHER ALUMINUM DIVISION

The Archer Aluminum division of the Company is one of the most complete and modern producers of packaging materials for consumer and industrial markets.

Three Archer plants, with more than a half million square feet of production, research, and warehouse space, employ approximately 700 people.

Archer's leadership in the rolling of wide light-gauge foil for converting has been further enhanced by its part in pioneering in the continuous casting of aluminum strip from the basic metal. This vertical integration of production facilities has reduced costs, increased flexibility of operations, and improved quality control.

In addition to aluminum strip casting, Archer's production processes include such widely varied operations as sheet and foil rolling and slitting; laminating and coating of numerous combinations of materials with aqueous, wax, and thermoplastic adhesives; polyethylene laminating and coating; printing, coloring, embossing, and die cutting; metal forming and bag making; and a host of related operations.

While the major part of Archer's production is for the Company's use in its tobacco business, sales to others have increased substantially. An intensive product development program, coordinated with the research and development efforts of Archer's customers, constantly searches for new and improved products and techniques.

AGRICULTURAL RESEARCH

In view of the Company's natural interest in assuring the production of an adequate supply of basic raw materials of superior quality, it has for a long time supported research related to the growing of tobacco.

Present areas of interest include development of the following:

- Suitable labor-saving devices for planting, cultivating, harvesting, and curing tobaccos;
- Improved cultural practices, including control of weeds and grasses and crop protection techniques;
- Knowledge concerning the effects which environmental and genetic factors have upon growth and quality of tobacco.

The Company provides financial support for selected projects at agricultural experiment stations in the major tobacco-growing states.

Farms owned by the Company in Bertie County, North Carolina, and near Lexington, Kentucky, are used for tobacco-farming experiments with flue-cured and Burley varieties.

The objective of the tobacco experiment program in Bertie County is to explore ways to help tobacco farmers improve their practices in growing, harvesting, curing, and preparing tobacco for the auction markets. This program is being conducted in collaboration with the North Carolina Agricultural Experiment Stations and N. C. State of the University of North Carolina at Raleigh. During the 1963 tobacco season, experiments were conducted in mechanized harvesting and bulk curing, and a number of alternative practices were studied and evaluated. Part of the experimental work is repeated at other locations in the eastern North Carolina area.

Company directors Kenneth H. Hoover, vice president and director of research (right), and D. Rice Allen, Jr., manager, leaf buying department, inspect progress of automated bulk curing of machine-harvested flue-cured tobacco at Company farm in North Carolina.

Work at the Kentucky farm was devoted largely to experiments with varieties of Burley tobacco developed at the University of Kentucky.

In the Company's own research laboratories the experimental tobacco crops are tested for smoking flavor and chemical qualities. For example, approximately 3,000 samples of experimental crops submitted by the various experiment stations were evaluated last year.

10 YEAR RECORD Condensed Comparative Financial Data

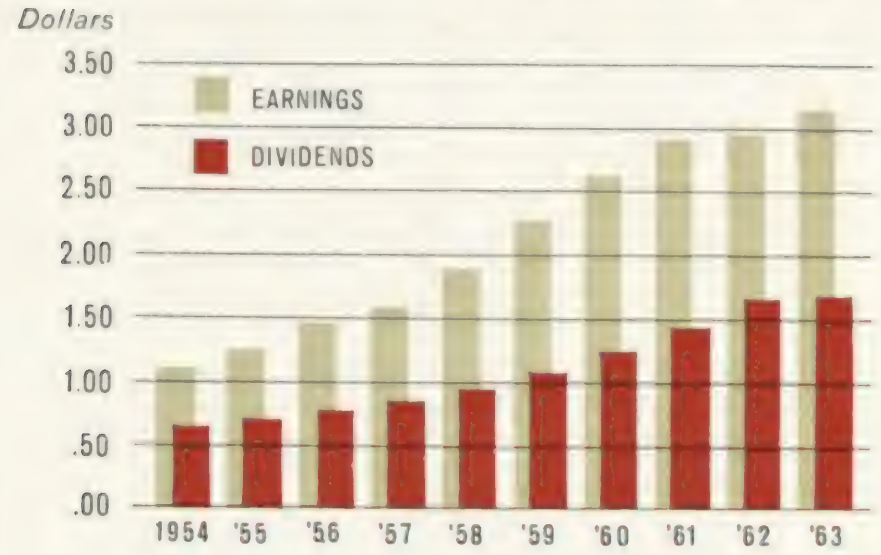
Prior years re-stated to include Pacific Hawaiian Products Company

R. J. REYNOLDS TOBACCO COMPANY AND CONSOLIDATED SUBSIDIARIES

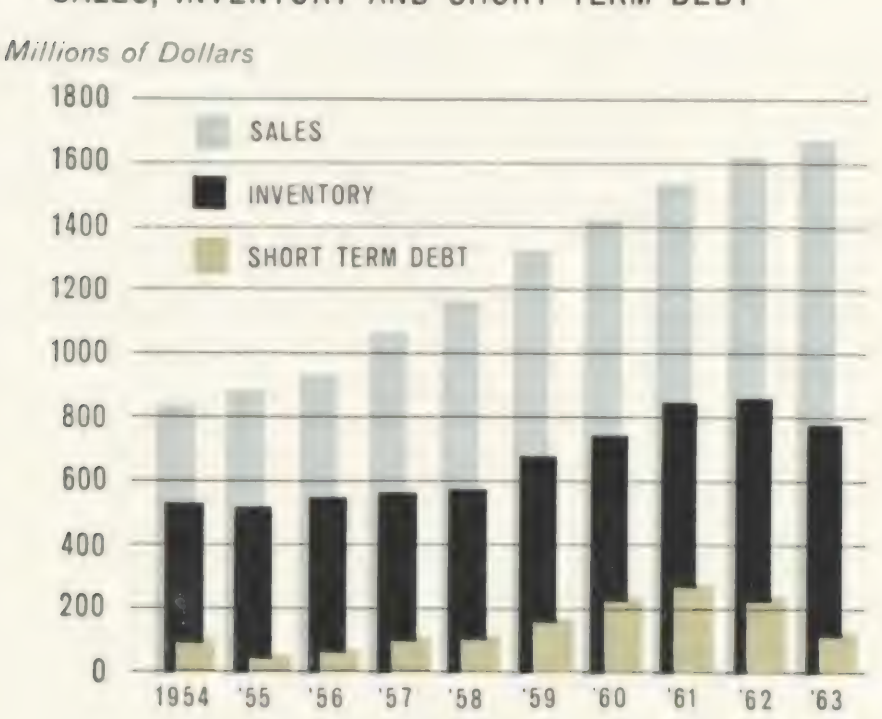
Year ended December 31,	1963	1962	1961	1960	1959
SALES, EARNINGS AND DIVIDENDS (amounts in thousands of dollars)					
Net Sales	$1,672,445	$1,627,541	$1,555,527	$1,438,547	$1,306,197
Income before taxes	277,601	260,977	265,220	224,018	199,825
Federal and state taxes on income	148,535	139,821	146,499	120,841	108,507
Net Earnings	129,066	121,156	118,721	106,375	91,318
Dividends on Preferred Stock	858	936	1,044	1,135	1,296
Dividends on Common Stock	67,602	64,512	56,439	48,345	42,260
FINANCIAL POSITION AND EQUITIES (amounts in thousands of dollars)					
Current Assets	$ 878,116	$ 930,246	$ 929,775	$ 827,224	$ 760,034
Federal and state tax liabilities	106,074	101,325	94,314	79,068	88,287
Other Current liabilities	151,922	260,508	293,414	248,374	191,636
Working Capital	620,120	568,413	542,047	499,782	480,112
Real Estate, Machinery and Equipment—Net	150,023	147,568	129,001	112,606	96,153
Total Assets	1,037,640	1,089,127	1,067,861	953,756	859,386
Funded Debt	68,000	74,000	80,000	86,000	92,000
Equity of holders of Preferred Stock	22,459	24,975	27,871	29,511	34,301
Equity of holders of Common Stock	689,185	628,320	572,262	510,692	453,234
FINANCIAL STATISTICS (Adjusted for 2-for-1 stock splits in 1961 and 1959 and, except for dividends per share on Common Stock, the acquisition of Pacific Hawaiian on a pooling of interests basis)					
Income taxes per share of Common Stock	$ 3.62	$ 3.41	$ 3.58	$ 2.95	$ 2.65
Earnings per share on Common Stock	3.13	2.93	2.87	2.57	2.20
Dividends per share on Common Stock	1.65	1.60	1.40	1.20	1.05
Book value per share of Common Stock	16.82	15.34	13.97	12.47	11.07

1958	1957	1956	1955	1954
$1,163,258	$1,066,727	$ 967,609	$ 872,580	$ 820,164
173,757	139,930	138,187	121,725	103,689
94,576	75,142	75,722	68,220	58,678
79,181	64,788	62,465	53,505	45,011
2,306	2,685	2,801	2,838	2,936
37,150	32,785	30,760	25,773	23,767
$ 665,337	$ 649,841	$ 613,678	$ 568,607	$ 575,421
75,683	64,300	71,684	69,780	62,433
132,137	117,179	77,121	52,519	83,232
457,517	468,362	464,872	446,309	429,756
79,830	64,376	45,799	42,246	41,035
748,329	717,333	662,861	614,386	619,882
98,000	104,000	110,000	115,000	120,000
37,666	67,012	69,033	71,386	74,077
404,849	364,842	335,022	305,701	280,139
$ 2.31	$ 1.84	$ 1.85	$ 1.67	$ 1.44
1.88	1.52	1.46	1.24	1.04
.92½	.82½	.77½	.65	.60
9.89	8.91	8.20	7.48	6.90

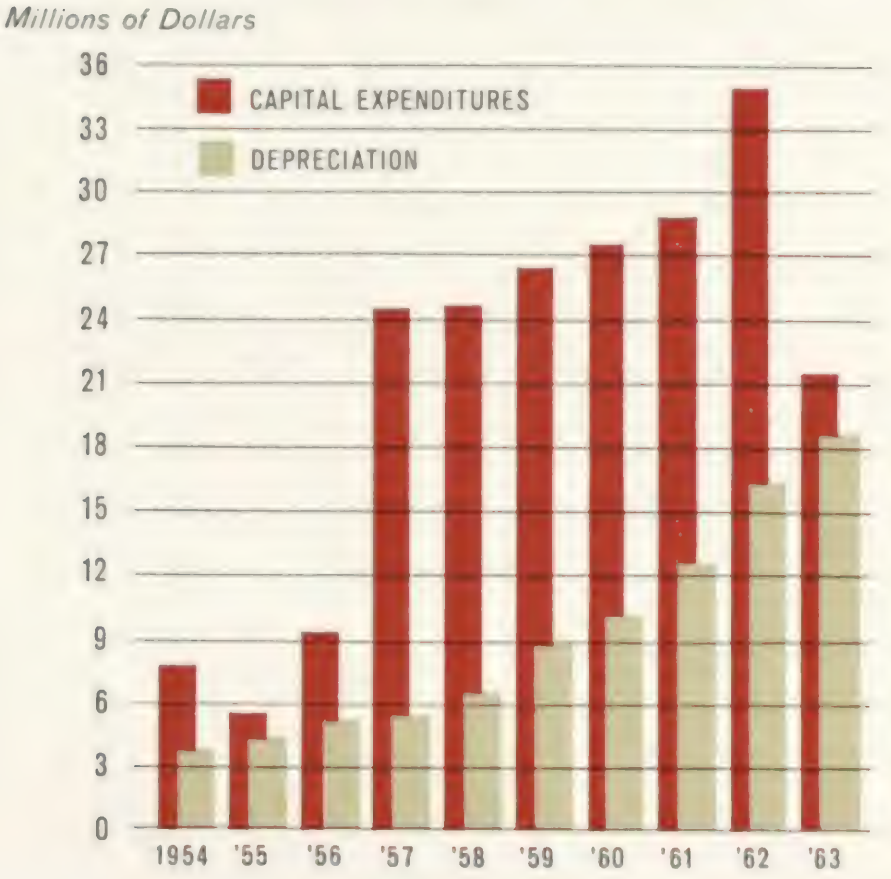
EARNINGS AND DIVIDENDS PER COMMON SHARE



SALES, INVENTORY AND SHORT TERM DEBT



CAPITAL EXPENDITURES AND DEPRECIATION



R. J. REYNOLDS
TOBACCO COMPANY
AND CONSOLIDATED
SUBSIDIARIES

FINANCIAL POSITION—

ASSETS	1963	1962
CURRENT ASSETS:		
Cash	$ 24,214,289	$ 30,305,757
Marketable securities—at cost (approximately equal to market)	1,193,278	520,462
Accounts receivable from customers (less discounts)	57,143,040	53,491,187
Leaf tobacco, supplies, manufactured products, etc.—at cost (substantially all on last-in, first-out basis)	795,565,237	845,928,451
TOTAL CURRENT ASSETS	878,115,844	930,245,857
REAL ESTATE, MACHINERY AND EQUIPMENT—at cost	239,964,050	225,417,598
Less allowances for depreciation	89,941,019	77,849,554
NET REAL ESTATE, MACHINERY AND EQUIPMENT	150,023,031	147,568,044
OTHER ASSETS:		
Investments in (at cost, less reserves) and advances to unconsolidated foreign affiliates	7,161,292	7,810,206
Other investments	413,675	505,953
Brands, trade-marks and good will	1	1
Prepaid expenses and sundry receivables	1,925,691	2,996,815
TOTAL OTHER ASSETS	9,500,659	11,312,975
	$1,037,639,534	$1,089,126,876

December 31, 1963 with comparative figures for 1962

LIABILITIES	1963	1962
CURRENT LIABILITIES:		
Notes payable	$ 114,500,000	$ 222,350,000
Accounts payable and sundry accrued accounts	31,721,506	32,157,217
Funded debt due within one year (less principal amount of debentures in Treasury—1963, $300,000)	5,700,000	6,000,000
Federal and state taxes	106,074,341	101,325,246
TOTAL CURRENT LIABILITIES	257,995,847	361,832,463
FUNDED DEBT (due in 1965, $6,000,000; annually 1966-1972, $7,000,000; 1973, $13,000,000):		
2½% Promissory Notes	23,000,000	28,000,000
3% Debentures, due October 1, 1973	45,000,000	46,000,000
TOTAL FUNDED DEBT	68,000,000	74,000,000
CAPITAL AND EARNINGS RETAINED:		
Preferred Stock—Par $100		
Authorized and issued 490,000 shares 3.60% Series	49,000,000	49,000,000
Common Stock—Par $5		
Authorized		
60,000,000 shares		
Issued		
40,971,533 shares	204,857,665	204,857,665
	253,857,665	253,857,665
Earnings Retained for requirements of the business	480,221,023	419,615,248
	734,078,688	673,472,913
Less Cost of Stock in Treasury:		
Preferred Stock, 3.60% Series		
(265,410 shares in 1963; 240,253 shares in 1962)	22,392,340	20,178,500
Common Stock (1,110 shares in 1963)	42,661	——
	22,435,001	20,178,500
TOTAL CAPITAL AND EARNINGS RETAINED	711,643,687	653,294,413
	$1,037,639,534	$1,089,126,876

R. J. REYNOLDS TOBACCO COMPANY AND CONSOLIDATED SUBSIDIARIES

STATEMENT OF EARNINGS

Year ended December 31, 1963—with comparative figures for 1962

	1963	1962
NET SALES	$1,672,444,707	$1,627,541,446
OTHER INCOME	920,222	464,921
TOTAL INCOME	1,673,364,929	1,628,006,367
LESS:		
Cost of goods sold, selling and general expenses, exclusive of items below	1,370,294,059	1,342,523,947
Provision for depreciation	18,338,525	15,648,401
Interest and debt expense	7,131,586	8,857,354
Provision for Federal and state taxes on income	148,535,000	139,820,500
TOTAL INCOME DEDUCTIONS	1,544,299,170	1,506,850,202
NET EARNINGS	129,065,759	121,156,165
Dividends paid on Preferred Stock	857,898	936,486
NET EARNINGS APPLICABLE TO COMMON STOCK	$ 128,207,861	$ 120,219,679

NOTES TO FINANCIAL STATEMENTS

NOTE A — PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its domestic subsidiaries. Foreign affiliates are not consolidated, such investments being carried at cost less reserves to reduce them to the equity in the underlying net book assets.

On February 14, 1963, the Company issued 971,533 shares of its Common Stock in connection with the acquisition by its wholly-owned Delaware subsidiary, Pacific Hawaiian Products Company, of the business and substantially all the assets of a California corporation having the same name. The combination has been accounted for on a "pooling of interests" basis with the accounts consolidated for the entire year 1963 and for comparative purposes for the year 1962.

NOTE B — OUTSTANDING STOCK OPTIONS

Pursuant to the agreement under which the Company's subsidiary made the acquisition referred to in Note A, such subsidiary issued to certain of its officers and employees on February 14, 1963, in substitution for outstanding options to purchase stock of the California corporation, options, expiring at varying dates to August 1, 1967, to purchase shares of Common Stock of the Company at prices per share as follows: 9,306 shares, $14.64; 686 shares, $15.51; 3,050 shares, $34.20; 2,775 shares, $37.80. In 1963 a substituted option for 235 shares was cancelled and substituted options for 4,758 shares were exercised. At December 31, 1963, substituted options were outstanding at option prices per share as follows: 4,541 shares, $14.64; 458 shares, $15.51; 3,050 shares, $34.20; 2,775 shares, $37.80.

R. J. REYNOLDS TOBACCO COMPANY AND CONSOLIDATED SUBSIDIARIES

STATEMENT OF EARNINGS RETAINED

Year ended December 31, 1963—with comparative figures for 1962

	1963	1962
EARNINGS RETAINED for requirements of the business—at beginning of year	$419,615,248	$365,189,164
ADD:		
Net Earnings	129,065,759	121,156,165
	548,681,007	486,345,329
DEDUCT:		
Cash dividends—		
R. J. Reynolds Tobacco Company:		
Preferred Stock, 3.60% Series	857,898	936,486
Common Stock at $1.65 per share for 1963 ($1.60 per share for 1962)	67,602,086	64,000,000
Pacific Hawaiian Products Company:		
Common Stock at $.30 per share	——	512,422
TOTAL CASH DIVIDENDS	68,459,984	65,448,908
Excess of Par Value of R. J. Reynolds Common shares issued for Pacific Hawaiian shares over the adjusted Capital of Pacific Hawaiian at December 31, 1961, and certain combination expenses	——	1,281,173
TOTAL DEDUCTIONS	68,459,984	66,730,081
EARNINGS RETAINED for requirements of the business—at end of year	$480,221,023	$419,615,248

REPORT OF INDEPENDENT ACCOUNTANTS

R. J. REYNOLDS TOBACCO COMPANY, ITS DIRECTORS AND STOCKHOLDERS

We have examined the statement of financial position of R. J. REYNOLDS TOBACCO COMPANY and consolidated subsidiaries as of December 31, 1963, and the related statements of earnings and of earnings retained for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We were present when inventories were taken by the Company and checked procedures followed in determining quantities and valuation.

In our opinion, the accompanying statement of financial position and statements of earnings and of earnings retained present fairly the financial position of R. J. Reynolds Tobacco Company and consolidated subsidiaries at December 31, 1963, and the results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Winston-Salem, N. C., February 5, 1964

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R. J. REYNOLDS TOBACCO COMPANY

BOARD OF DIRECTORS

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CHARLES H. BABCOCK
LEIGHTON H. COLEMAN
A. H. GALLOWAY
BOWMAN GRAY
GORDON GRAY
S. B. HANES, JR.
KENNETH H. HOOVER
WILLIAM R. LYBROOK
DAVID S. PEOPLES
H. H. RAMM
JOSEPH H. SHERRILL
W. S. SMITH, JR.
COLIN STOKES
CHARLES B. WADE, JR.

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BOWMAN GRAY . . . . . *Chairman, Board of Directors*
A. H. GALLOWAY *President and Chairman, Executive Committee*
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COLIN STOKES . . . . . *Executive Vice President*
H. H. RAMM . . . . . *Vice President*
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CHARLES B. WADE, JR. . . . . *Vice President*
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WILLIAM R. LYBROOK . . . . *Vice President and Secretary*
JOSEPH H. SHERRILL . . . . . *Vice President*
DAVID S. PEOPLES . . . . . *Comptroller*
E. C. PETERSON . . . . . *Treasurer*

REGISTRAR

MANUFACTURERS HANOVER TRUST COMPANY
350 Park Avenue, New York 22, N. Y.

TRANSFER AGENTS

THE CHASE MANHATTAN BANK
1 Chase Manhattan Plaza, New York 15, N. Y.

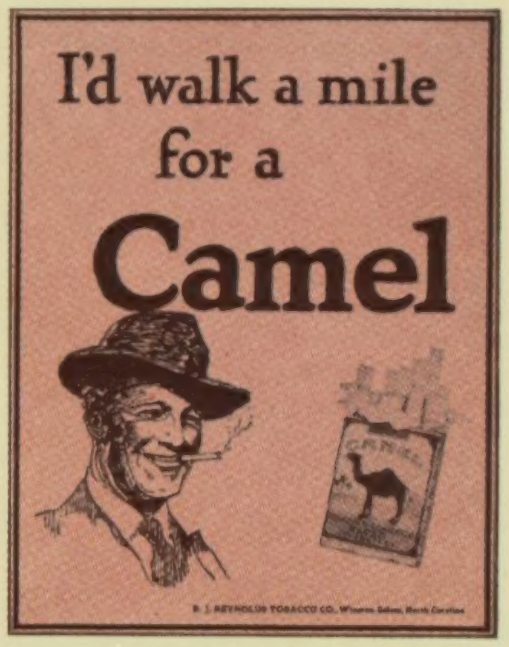
THE FIRST NATIONAL BANK OF JERSEY CITY
1 Exchange Place, Jersey City 3, N. J.

50th Anniversary of a great cigarette

On October 3, 1913, the first sale of CAMEL cigarettes was made. CAMEL was a real innovation, for it combined flue-cured, Burley, and Turkish tobaccos for the first time. "The first truly American cigarette," one historian has called it. By 1915 CAMEL had become one of the country's most important brands. CAMEL was one of the first cigarettes to be sold without premiums, a policy it has always maintained. It was the first to be wrapped in moisture-proof cellophane. Today CAMEL represents one of the best-known trademarks in the entire world. More CAMELS are sold than any other regular-size cigarette.

CAMEL was the first cigarette to be advertised with an intensive national campaign. Here are examples of three themes from "the first 50 years."

1913



1923

1963

BLK. RT.
ADV'L. 1/4¢ PD.

WINSTON-SALEM N.C.
U.S. POSTAGE
02
PB METER
PB. 187000

RJR

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Winston-Salem/North Carolina

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put Winston in a league by itself. For the best taste
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